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OUTLOOK 2020:
WORLDWIDE EQUITIES STILL HAVE UPSIDE POTENTIAL, US BULL MARKET TO CONTINUE

Although the world economy is certainly not in perfect condition, a global recession is not to be expected in 2020. Global equity markets continue to benefit from very good fundamentals and the technical picture gives reason to hope for a further upside. Compared to bonds, equity valuations are still promising, especially considering that corporate profits can be expected to rise again this year. As in previous years, the US equity market offers the biggest opportunities for investors, although the US election campaign could prove to be the greatest risk.

The world economy is divided: Whereas consumer spending and services are strong, manufacturing is mired in a crisis. In the United States, for example, the ISM Manufacturing Index has recently fallen well below the crucial mark of 50. Above all, the manufacturing sector has been weighed down by political problems, especially the trade dispute between the United States and China. "We hope that global manufacturing will stabilise somewhat in 2020", said Till Christian Budelmann, Capital Markets Strategist of the Swiss private bank Bergos Berenberg. Although political uncertainty remains high, there have been some positive developments. For one, the partial agreement ("phase-one deal") between the United States and China can be expected to alleviate trade tensions for now. And the tensions surrounding Brexit, which will most probably happen at the end of January, have also eased somewhat. "Although the US-Iran conflict has worsened since the beginning of the year and is undeniably a moral problem, we still consider it to be more of a political issue without that much influence on the economy, from the standpoint of investors. That would change, of course, if war actually broke out", Budelmann said.

Budelmann does not expect a global recession in 2020. Bergos Berenberg is forecasting 1.0 and 5.9 percent economic growth this year for the Eurozone und China, respectively, more or less in line with the consensus estimate. Regarding the United States, the private bank is more optimistic than the average opinion of economists, predicting 2.1 percent growth in 2020. Despite the generally positive economic outlook, Budelmann does not expect a reversal of interest rate policy anytime soon. On the contrary, central banks across the world will support markets with expansive monetary policy in 2020. However, the US central bank will probably not cut interest rates further this year, according to Budelmann.

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MODERATE PROFIT GROWTH AND YIELD ADVANTAGE OVER BONDS

After the unusually strong growth in 2018, corporate profits were essentially flat in 2019 and actually appear to have declined a little in Europe. Nevertheless, equity prices increased substantially, with global equities gaining around 25 percent last year. As a result, equity valuations increased as well, begging the question. Are equities too expensive now? “While they are not as cheap as they were a year ago, they are still undervalued compared to bonds,” Budelmann said. The difference is even greater in Europe. The price-earnings ratio of the MSCI World Index is roughly at the average level of the past 30 years. The yield gap with bonds is still attractive. “For example, if you subtract the yields of 10-year US Treasuries from S&P 500 dividend yields, you will come up with a difference of 3.6 percentage points right now”, Budelmann explained. Moreover, he expects worldwide profit growth in 2020, although he thinks that the prevailing analysts’ estimate of 10 percent at the beginning of this year is too high. He considers the forecast global sales growth of 4 to 5 percent to be realistic, but he expects stagnating profit margins, in contrast to the consensus expectation. “This together with stock buybacks and an accustomed dividend yield seems to be a positive fundamental basis for equities this year”, Budelmann said.

TECHNICAL ANALYSIS SUPPORTS FUNDAMENTAL VIEW FOR EQUITIES IN 2020

His general view is confirmed by chart-technical analysis. After moving sideways for the third time since the financial crisis, the 200-day moving average of the US stock index S&P 500 has already turned up again, fuelling hopes for another upward phase. In Europe, the Stoxx 600 is at an interesting point, at the level of its all-time high last reached in 2000, 2007, and 2015. “If it can rise significantly above this level, that could trigger strong follow-on buying”, Budelmann predicted.

He sees a potential, albeit so far limited risk of capitulation by the bears. “Already now, the positioning of market participants is no longer as defensive as it had been. If investors who have long been pessimistic and cautious now pile into equity markets to a greater degree, that would be good for the markets in the short term, but would potentially pose a risk in the medium term. The currently advantageous combination of attractive valuations and pessimistic sentiment would then be gone”, Budelmann said.

Budelmann continues to prefer the US equities market: “Corporate profits are still rising faster there than in the rest of the world. We expect the bull market to continue in 2020, extending the US rally into its 12th year.” He now takes a more positive view of Europe, after the region was upgraded to neutral already at the end of 2019. Emerging markets are still underweighted.

US ELECTIONS ARE CRUCIAL AND REPRESENT THE GREATEST RISK IN 2020

In Budelmann's opinion, the US election campaign will exert a strong influence not only on the US equity market, but on markets in general. He considers a re-election of Donald Trump to be neutral or modestly positive for the market because the tax reduction and deregulation policies would continue, although that would also mean continued trade stress. He takes a similar view of the election of a centrist Democrat like Joe Biden, Pete Buttigieg, or Michael Bloomberg, which would mean less trade stress, though it would also mean an end to supply-side advantages. Budelmann views an election victory of left-leaning Democrats Bernie Sanders or Elizabeth Warren as problematic for markets. "This would be especially negative if it also came with a Democrat majority in the Senate and the House of Representatives. That would lead to more regulation and higher taxes. Such a scenario represents the biggest risk to our moderately positive 2020 market outlook", Budelmann said.

He considers the impeachment process that is currently dominating the headlines to be irrelevant for markets. Despite all the hype, he considers it nearly impossible that President Trump will not serve out his first term for any reasons other than health.

TILL CHRISTIAN BUDELMANN

As capital market strategist of the private bank Bergos Berenberg, Till Christian Budelmann regularly comments on events on the international capital markets and examines them in the context of economic and political trends. Since 2004, Budelmann has been responsible for various investment strategies and sits on the bank's Investment Committee. He has been Managing Director since 2013.

MARKET COMMENTARY

Zurich, 15 January 2020

BERGOS BERENBERG AG

Bergos Berenberg AG is an independent Swiss private bank with headquarters in Zurich and offices in Geneva. It emerged from Joh. Berenberg, Gossler & Co. KG, it has been active in the Swiss financial centre for international private clients and entrepreneurs for over thirty years. The Swiss private bank specializes in asset management and advisory services. For its more than 100 employees, the focus is on providing advice in all known liquid and non-liquid asset classes, as well as in alternative investments such as real estate, private equity or art. It provides entrepreneurial clients with access to M&A and other corporate finance services. Bergos Berenberg AG offers private clients, entrepreneurs and their families a holistic service spanning several generations, which, in addition to investment recommendations, aims at security, neutrality, internationality and cosmopolitanism.

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